

IN THE COURT OF APPEALS OF TENNESSEE
AT NASHVILLE
September 10, 2008 Session

**STATE EX REL. LITTLE PEOPLE'S CHILD DEVELOPMENT
CENTER, INC. v. LITTLE PEOPLE'S CHILD DEVELOPMENT
CENTER, INC., ET AL.**

**Appeal from the Chancery Court for Davidson County
No. 01-985-I Claudia C. Bonnyman, Chancellor**

No. M2007-00345-COA-R3-CV - Filed January 9, 2009

WillieAnn Madison and her husband, John Madison (“Defendants”), operated Little People’s Child Development Center, Inc. (“Little People’s”), a Tennessee nonprofit corporation which provided child daycare services. Over the years, Defendants treated the nonprofit as their for-profit corporation, retaining for their personal use millions of dollars of the nonprofit’s proceeds. The Tennessee Attorney General (“the State”) filed suit on Little People’s behalf seeking to recover money used by Defendants for personal gain. Following a partial summary judgment and then an extended trial, the Trial Court entered a detailed judgment against Defendants for over \$2.2 million. The Trial Court, however, dismissed the State’s claim seeking compensation for the value of the nonprofit at the time the nonprofit was dissolved and Defendants transferred any remaining assets to their new limited liability company. Defendants appeal claiming various items and amounts should not have been included in the Trial Court’s final judgment. The State appeals claiming the Trial Court erred when it dismissed its claim seeking compensation for the value of the nonprofit at the time of dissolution. We affirm the judgment of the Trial Court with respect to the issues raised by Defendants. We agree with the State that the Trial Court erred when it dismissed the State’s claim seeking a judgment for the value of the nonprofit at the time of dissolution. The judgment of the Trial Court is, therefore, affirmed in part, reversed in part, and remanded for further proceedings consistent with this opinion.

**Tenn. R. App. P. 3 Appeal as of Right; Judgment of the Chancery Court
Affirmed in Part and Reversed in Part; Case Remanded**

D. MICHAEL SWINEY, J., delivered the opinion of the court, in which FRANK G. CLEMENT, JR., J., and SHARON G. LEE, SP. J., joined.

Larry B. Hoover, Nashville, Tennessee, for the Appellants, WillieAnn Madison and John Madison.

Robert E. Cooper, Jr., Attorney General and Reporter, Dennis J. Garvey, Deputy Attorney General, and George S. Bell, III, Senior Counsel, Nashville, Tennessee, for the Appellee, State of Tennessee *ex rel.* Little People's Child Development Center, Inc.

OPINION

Background

This lawsuit was filed in April 2001 by the Tennessee Attorney General on behalf of Little People's. In a nutshell, the State was seeking to recover assets on behalf of Little People's which the State claimed had been improperly used by the defendants. More specifically, the State claimed that the defendants had treated the nonprofit corporation for several years as if it were a for-profit corporation and spent most of the nonprofit corporation's assets. The State sued WillieAnn Madison, who primarily was responsible for operating the nonprofit corporation. The State also sued John Madison, who is WillieAnn Madison's husband, as well as William Davis¹, Phyllis Herring², and Little People's Preparatory Academy, LLC.³ According to the complaint:

[The] Attorney General . . . is the chief law enforcement officer of this State. He has common law and statutory powers to enforce state law and to protect the public's interest in Tennessee public benefit corporations. Tenn. Code Ann. §§ 48-64-301 and 48-64-303.

Little People's Child Development Center, Inc., (Little People) is a public benefit corporation organized under the Act. It has no members. Its principal place of business is located at 4933 Fairley, Memphis, Shelby County, Tennessee. It is a tax exempt organization.

¹ William Davis is WillieAnn Madison's father. Davis was found jointly and severally liable for the full amount of the judgment rendered against WillieAnn Madison and James Madison. Davis did not file a proper notice of appeal and his appeal was dismissed. Accordingly, the judgment against Davis is not at issue on this appeal. Any reference in this Opinion to "Defendants" refers to WillieAnn Madison and John Madison, unless indicated otherwise.

² Phyllis Herring is WillieAnn Madison's sister. Herring admitted that she signed a \$26,000 promissory note in favor of Little People's with no provision for a repayment schedule or payment of interest. Accordingly, a \$26,000 judgment was entered against Herring and that judgment was not appealed.

³ Little People's Preparatory Academy, LLC (the "LLC"), was formed by the Madisons following the dissolution of Little People's Child Development Center, Inc. The State sued the LLC because it claimed many of Little People's remaining assets were improperly transferred to the LLC after dissolution of the nonprofit corporation.

John E. Madison, Sr. is the president and a director of defendant Little People.

William H. Davis is the secretary and a director of defendant Little People.

Little People's Preparatory Academy, LLC (Preparatory Academy) is a for-profit Tennessee limited liability company. Its principal place of business is located at 4933 Fairley, Memphis, Shelby County, Tennessee. . . .

Upon information and belief, WillieAnn Madison and John E. Madison, Sr. are Owners/Members of defendant Preparatory Academy. . . .

On or about November 9, 2000, a Civil Investigative Demand was served upon defendant Little People by plaintiff pursuant to Tenn. Code Ann. §§ 8-6-401, *et seq.* . . . As of this date, defendant has failed to comply completely with this demand, which requested among other things, financial information. . . .

On or about February 12, 2001, Debbie Renee Ruffin, John Madison and WillieAnn Madison filed on behalf of defendant Preparatory Academy an "Application For A License To Operate A Child Care Agency" with the Tennessee Department of Human Services (DHS). . . . WillieAnn Madison and John Madison are listed on the application as "owners" of defendant Preparatory Academy. On or about February 15, 2001, DHS announced its intention to issue defendant Preparatory Academy a license at 4933 Fairley.

On or about February 27, 2001, defendant Little People filed Articles of Dissolution with the Secretary of State. Pursuant to Tenn. Code Ann. § 48-64-104, defendant Little People was required to . . . give the Attorney General written notice of its intent to dissolve at or before the time it delivered the articles of dissolution to the Secretary of State. Defendant Little People did not do so. . . .

On March 7, 2001, plaintiff received a notice regarding defendant's intent to dissolve. . . . Upon receipt of this notice, the Attorney General immediately sent to defendant's counsel the standard nonprofit packet requesting information needed to perform his statutory duties. . . .

On March 27, 2001, plaintiff denied authorization to dissolve. Defendant has failed or refused to respond to the request for information, to execute a valid extension agreement, or to submit an adequate plan of dissolution. . . .

Defendants have failed to render a full and proper accounting of the assets once held by the nonprofit. For example, defendant Little People fails to account for its tangible and intangible assets of defendant. In its “plan,” defendant provides only for the distribution of about \$38,675 worth of vehicles, furniture and toys. . . .

In addition to failing to properly account for the nonprofit’s assets, defendants engaged in various related party transactions, including without limitation, the leasing of real property from Madison, *to wit*: 1647 Semmes, 3272 Chelsea, 4925 Fairley, 4933-4935 Fairley, and 2845 Mendenhall. . . . These leases reflect a pattern of unexplained renegotiation to pay unwarranted rent increases.

Upon information and belief, nonprofit assets of defendant Little People have inured to the private benefit of John Madison and WillieAnn Madison, both directly and indirectly through defendant Preparatory Academy.

Defendant Preparatory Academy is currently operating a child care agency at 4933 Fairley and 2845 Mendenhall. Nonprofit assets of defendant Little People have been improperly transferred to the custody or control of defendant Preparatory Academy without the approval of the Attorney General. Said assets are currently being utilized for its private benefit. Such transfer was outside the regular course of defendant Little People’s activities.

Pursuant to Tenn. Code Ann. § 48-62-102, defendant Little People is required to give the Attorney General at least twenty (20) days written notice before it sells, leases, exchanges or otherwise disposes of all, or substantially all, of its property in a transaction not in the usual course of its activities. Defendant Little People did not do so. (Original paragraph numbering omitted).

The State’s complaint sought a court order which, among other things: (1) enjoined or reversed the unauthorized voluntary dissolution; (2) reversed the unapproved merger of Little People’s and the LLC; (3) reversed the unapproved transfer of nonprofit assets; (4) reversed the illegal distribution of nonprofit assets; (5) required a proper accounting of Little People’s assets; and (6) judicially dissolved Little People’s.

While this litigation was proceeding, the State filed a motion for summary judgment, which the Trial Court granted in part. The relevant portion of the summary judgment memorandum opinion is as follows, with most footnotes being omitted but those few that are in the quoted text are in the original, although renumbered:

In April 1992, Little People was recognized as an I.R.C. 501(c)(3) organization. As described in its I.R.C. 501(c)(3) application, Little People was to provide “full-time daily child care services for children away from their home.” Little People’s purpose, as stated in its charter, was:

exclusively religious, charitable, scientific, literary, and educational within the meaning of section 501(c)(3) of the Internal Revenue Code of 1986 or the corresponding provision of any future United States Internal Revenue law ... this organization shall not carry on any activities not [permitted] to be carried on by any organization exempt from federal Income Tax under Section 501(c)(3) of the Internal Revenue Code....

The Court does not find other purposes of Little People in the record. Little People received state and federal funding, but the exact nature and amount is not in the record. The nonprofit did not have a budget. Its Board of Directors was inactive as regards formal management decisions but the Madisons were active in the transfer of Little People resources. Ms. Madison controlled Little People’s checkbook and had signature authority on the account. Ms. Madison also used Mr. Madison’s facsimile signature on Little People’s checks. Little People paid Mr. Madison an annual salary of \$52,000 as Executive Director of Little People.

Little People conducted its day care business at the following locations owned by the Madisons and Defendant Phyllis Herring, Ms. Madison’s sister: 1647 Semmes, 3272 Chelsea, 4933 Fairley, and 2845 Mendenhall. Since 1991, Little People contracted to pay the Madisons not less than \$1.4 million in rent.⁴ The Madisons purchased 4280 Cherry Center Drive for use in the Cherokee-Services

⁴ The Madisons do not dispute this calculation but assert their Fifth Amendment rights with respect to amounts that were actually paid as rent or in lieu of rent.

business.⁵ Little People paid \$5,653.18 on this property's mortgage to First Savings Bank and paid at least \$9,854.87 to Citicorp for the Semmes mortgages.

Little People paid WillieAnn Madison's American Express charges totaling approximately \$72,388.79. Much of this expense was personal. Undisputed [personal] expenses for travel from Nashville include:

1. October 1993, travel to New York, NY: \$1,194.59.
2. October 1993, travel to Detroit, MI: \$1,437.00.
3. August 1994, travel to New York, NY: \$1,008.00.
4. August 1994, travel to Seattle, WA: \$1,168.50.
5. September 1994 and September 1995, travel to Washington, D.C.: \$2,465.64.
6. July 1995, travel to Charlotte, N.C.: \$1,008.00.
7. June 1996, travel to Chicago, IL: \$1,235.00.
8. Cost for Ms. Madison's daughter, Chaun Daughtry, to travel home from college: \$1,862.00.

Personal travel expenses incurred on the American Express credit card totaled \$17,911.28. Payments totaling \$5,351.19 from Little People's corporate checking account paid Ms. Madison's personal credit account with Saks Fifth Avenue. Little People paid \$15,118.23 on Ms. Madison's personal credit card account with Bank of America and \$6,601.17 on her Goldsmiths personal account. Other personal bills paid by Little People include medical payments of \$8,830.07, payments totaling \$51,704.54⁶ towards health care costs [or] medicine, \$1,720.00 to A/E Designers-Consultants, \$1,575 to A.M. Pool Services, and \$963.30 to Prepaid Legal. Little People

⁵ Cherokee Children and Family Services, Inc. and Cherokee Children Nutrition, Inc. were two nonprofit public benefit corporations that abandoned their charitable purposes. *See Summers v. Cherokee Children & Family Services, Inc.*, 112 S.W.3d 486, 500 (Tenn. Ct. App. 2002).

⁶ Little People did not pay for employees' life/health insurance.

made payments to American Marketing totaling \$17,292.75 for indefinite purposes.

Little People purchased vehicles which were titled to the Madisons or their family members. The non-profit paid personal utility bills at numerous locations including the Madisons' residence. Little People loaned \$500 to Mr. Madison's former sister-in-law and paid \$26,000 to Ms. Madison's sister, Phyllis Herring. Little People loaned Mt. Zion A.M.E. Church \$3,000 and another \$10,000 for a church program. No interest was charged and no purpose known.

Little People's payments of the Madisons' credit card debt ... were described in detail in the Attorney General's Statement of Material Facts, filed pursuant to Tenn. R. Civ. P. 56. Facts numbered 116 through 158 recount numerous occasions when Little People was caused, by the Madisons, through credit card payments or otherwise, to pay the personal bills incurred by John E. Madison, Sr. and WillieAnn Madison. These numbered facts also recount occasions when the Madisons caused Little People to distribute charitable funds directly to themselves. In compliance with Tenn. R. Civ. P. 56, each fact is supported by a citation to the record, usually to notices of filing with certain documents attached.

Importantly, the responses filed by the Madisons to the facts numbered 116 through 158, admit the charges and expenses incurred. The Madisons raise a continuing objection to all the facts: "the facts do not establish that all travel expenses and payments involved personal expenses." This continuing objection to facts numbered 116 through 158, does not provide citations to the record as required by Rule 56, so as to create a genuine dispute and except for the continuing objection, the Madisons agree with the fact statements. Given the rules for summary judgment practice, it is appropriate to deem facts numbered 116 through 158 in the Statement of Undisputed Facts filed by the Attorney General on March 17, 2004, undisputed or admitted.

There are other reasons for deeming statements 116 through 158 undisputed. The Madisons were ordered on January 21, 2004, to provide an accounting so that the Court could evaluate expenditures by Little People. The Madisons failed to comply with the order to account and have provided no information to aid the Court in determining which expenditures were justified for charitable purposes, or were expended illegally for the comfort and enrichment

of the Madisons. The Court requested and then ordered the Madisons to carry their burden as fiduciaries, but they declined every opportunity to do so. In addition, they objected to discovery of documents based upon privilege but refused to provide a privilege log or to otherwise identify the papers to be accorded protection.

Tenn. R. Civ. P. 26.02(5) requires the party make the claim of privilege expressly and “shall describe the nature of the documents, communications, or things not produced or disclosed...” so that the other party may assess the privilege protection. On February 18, 2004, the Madisons responded that all records had been provided to the Receiver (but did not claim that the Receiver was withholding access to the records), and asserted their 5th Amendment privilege and marital privileges. The Court is entitled to assume an adverse inference against the Madisons as to these requests. “[T]he Fifth Amendment does not forbid adverse inferences against parties to civil actions when they refuse to testify in response to probative evidence offered against them....” *Baxter v. Palmigiano*, 425 U.S. 308, 318 (1976); *see also Rachels v. Steele*, 633 S.W.2d 473 (Tenn. Ct. App. 1981).

This Court concludes the Madisons have a duty by law, as fiduciaries, to render an accounting of conflict of interest transactions. *Summers v. Cherokee Children & Family Services, Inc.*, 112 S.W.3d 486, 500 (Tenn. Ct. App. 2002). This duty is independent of the lawsuit and is independent of discovery in this matter. Requiring an officer or director of a nonprofit corporation to account for conflict of interest transactions is a logical and necessary consequence of the duty of an officer or director of full disclosure and of obtaining approval of conflict of interest transactions. The State, in seeking an accounting, was holding the Madisons to their legal obligations as officers and directors.

Additionally, the Court concludes that it was not violative or repugnant to the Madisons’ Fifth Amendment rights against self-incrimination to order the accounting nor was it unfair. A narrowly tailored invocation of the Fifth Amendment by the Madisons on specific items in the accounting would balance protection to the Madisons’ Fifth Amendment rights with the need to respond to this lawsuit. As explained in *Rachels v. Steele*, 633 S.W.2d 473 (Tenn. Ct. App. 1981) *citing U.S. v. White*, 589 F.2d 1283, 1287 (5th Cir. 1979):

Any “waiver” of the fifth amendment must be voluntary, but invocation of the privilege does not release defendant from any choice concerning the use of his or her testimony. The fifth amendment preserves the right to choose, and the voluntariness of the choice is always affected in some way by the exigencies of a particular situation. The voluntariness inquiry necessarily incorporates an understanding that defendant cannot be free from conflicting concerns, and in any case, defendant must weigh the relative advantages of silence and explanation. . . .

The Madisons defend that Tenn. Code Ann. § 48-58-601 bars any claims of breaches of duty or violations of the Act that occurred more than three years prior to initiating this action. Further, the Madisons argue that the fraudulent concealment exception to Tenn. Code Ann. § 48-58-601 is not applicable because Plaintiff did not plead fraud pursuant to Tenn. R. Civ. P. 9. Tenn. Code Ann. § 48-58-601 is not a bar to claims in this action because the statute does not apply to Plaintiff, the Tennessee Attorney General. “It is a well settled principle of law that Statutes of Limitations against the State as the sovereign, are looked upon with disfavor, and will not be enforced unless there is clear and explicit authority therefor given by statute.” *Anderson v. Security Mills*, 133 S.W.2d 478, 480 (Tenn. 1939). Tenn. Code Ann. § 48-58-601(a) does not specifically apply to the Attorney General nor does it specifically apply to the recovery of nonprofit corporation assets for the public interest. Furthermore, Tenn. Code Ann. § 48-51-701 of the Nonprofit Corporations Act, which is entitled “Attorney general and reporter,” provides that the power of the Attorney General to enforce the Nonprofit Act cannot be waived or otherwise lost. The Attorney General’s cause of action involving numerous personal payments from charitable funds and public monies, is not barred by the Statute of Limitations.

* * *

“A basic distinction between for profit and nonprofit entities is the possibility of private enrichment. Thus, ‘in general terms, a nonprofit enterprise in an organization in which no part of the income is distributable to its members, directors, or officers....’” *Summers v. Cherokee Children & Family Services, Inc.*, 112 S.W.3d 486, 500 (Tenn. Ct. App. 2002)(quoting Ronald Lee Gilman, Tennessee Corporations § 11B-1(2001)). Conflict of interest transactions between a director or officer and the corporation are subject to close

scrutiny. *Id.* at 504. Tenn. Code Ann. § 48-58-302(a) defines a conflict of interest transaction as “a transaction with the corporation in which a director or officer of the corporation has a direct or indirect interest.”

The Madisons dispute the existence of conflict of interest transactions and defend pursuant to Tenn. Code Ann. § 48-58-302, that the transaction were fair at the time they were entered into. The Madisons have not in any way, however, provided facts to demonstrate that these transactions were fair, and the record declares otherwise. A statement that the transactions are fair is a conclusory statement and not a material fact which avoids summary judgment. Disputed facts must be stated and then supported by citation to the record. *See* Tenn. R. Civ. P. 56.03. The Madisons do not supply such a defense.

The record reflects that nonprofit assets have benefitted the Madisons personally with no benefit to the charitable purpose. The issue is whether Little People complied with the requirements of the nonprofit public benefit corporations in fulfilling a charitable purpose or whether it was operated for private financial gain. *Summers v. Cherokee Children & Family Services, Inc.*, 112 S.W.3d 486 at 525. As the Court of Appeals recognized in *Cherokee*, I.R.C. 501(c)(3) exempts from taxation “corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes” and requires that “no part of the net earnings of [the exempt organization] inures to the benefit of any private shareholder or individual.”

After careful review of the record, and careful application of the Tennessee Rules of Civil Procedure, the Court summarily finds that the Madisons are liable to Little People for its nonprofit assets, taken for their private gain, and that the Madisons’ illegal and personal use of the nonprofit assets caused Little People to abandon its charitable purpose. The Court finds that Little People made the payments described by Statements of Undisputed Facts numbered 116 through 158 for the Madisons’ personal needs. The payments total \$355,538.60.

* * *

The Court also finds that Little People's nonprofit assets were transferred to the Preparatory Academy. Plaintiff asserts that the Preparatory Academy must be judicially dissolved pursuant to Tenn. Code Ann. § 48-245-901. A hearing must be set to address detailed information about nonprofit transfers to the Preparatory Academy, and to resolve Preparatory Academy's corporate status.

The Court denies summary judgment regarding the real property transactions and the assessment and collection of rent from Little People. These transactions are too complex and opinion oriented to establish through summary judgment and they must be set for trial.

The Madisons and the Preparatory Academy hold Little People's nonprofit assets in constructive trust. . . .

The Plaintiff is granted summary judgment against John E. Madison, Sr. and WillieAnn Madison jointly and severally in favor of Little People in the amount of \$355,538.60. The balance of the relief sought by the Plaintiff is reserved for trial.

Following the entry of this partial summary judgment to the State, an extensive trial took place between September 11 and 18, 2006. Following the trial, the Trial Court entered a detailed and considered final judgment. After reviewing the basic underlying facts set forth in its previous grant of partial summary judgment, the Trial Court stated as follows in its final judgment⁷:

As determined in *Summers vs. Cherokee Children and Family Services*, 112 S.W.3d 486 (Tenn. Ct. App. 2001), there is no prohibition on a nonprofit corporation conducting enterprises for income or for accumulating earnings, but such revenues must be used for purposes set out in the charter. There must be no monetary or pecuniary gain to the incorporators or members or directors, and no distribution of income or profits to them. A nonprofit corporation is prohibited from transferring assets, income or accumulated revenue to any individual who is a member or director or officer of the corporation. It is the unmistakable legislative intent that the nonprofit corporation's entitlement to a federal tax exemption depends on meeting certain common law standards of charity. Namely, an

⁷ Although most footnotes have been omitted, any footnotes contained within the quoted text of the final judgment are renumbered but otherwise are in the original.

institution's tax exempt status must serve a public purpose and not be contrary to the established public policy.

The duty of loyalty imposed on a for-profit corporation is defined differently than the duty imposed on a nonprofit. Policies and directors of a for-profit corporation are to be guided by their duty to maximize long-term profit for the benefit of the corporation and their shareholders, whereas a nonprofit public benefit corporation's reason for existence is not to generate a profit, and thus a director's duty of loyalty lies in pursuing or ensuring pursuit of a charitable purpose or public benefit, which is the mission of a nonprofit corporation.

Conflict of interest transactions between a corporation and a director or officer are subject to close scrutiny. The burden of proof to show fairness of any transaction is placed upon the officer or director because of his fiduciary duties and capacity. Tenn. Code Ann. § 48-58-302(a). From the founding of the daycare center as a public charity, WillieAnn Madison, and later John Madison, operated Little People, the nonprofit, as if it were their personal business. They did not separate the financial activities, but ran the nonprofit for their personal financial transactions.

Little People does not have owners or stockholders. It is managed by a board of directors who are accountable to the general public for the operation of the organization. The members of the board are to approve the operating policies of the organization and to approve the compensation of the operations officers. If the nonprofit board does not approve compensation, the corporation does not have the authority to pay any compensation. There were no board of directors meetings maintained for Little People. There were no authorizations for the payment of compensation. There were no authorizations for rental agreements of property owned by WillieAnn Madison, nor for mortgage payments on property owned by WillieAnn Madison.

John Madison was a Certified Public Accountant, and he testified that he completed a continuing education program on nonprofit accounting. Mr. Madison was made aware of the responsibilities of spending resources for the charitable purposes of this nonprofit. He was also aware of the obligation to maintain appropriate records of non-financial transactions. He simply decided not to confront his spouse as she conducted the business of Little People.

Although there were no board meetings, the Court finds that the directors, namely William Davis and John Madison, agreed that the nonprofit could be run as determined by WillieAnn Madison. Therefore, it follows that WillieAnn Madison was a director in fact. Even if the directors had approved all of these expenditures that are at issue in this case, the approval simply removes the voidability of the transaction by the corporation.

Directors considering approval of conflict-of-interest transactions, that is, transactions that benefit a family member, themselves, other directors or officers, must comply with their fiduciary duties in deciding whether to approve such transactions. The approval does not obviate the requirements that distributions must not be made to corporate insiders, and assets belonging to the nonprofit corporation must be used only for the public benefit purposes. Tenn. Code Ann. § 48-58-304 provides that a director who votes for or assents to a distribution made in violation of the Nonprofit Corporation Act, and does not comply with the standards of conduct established in Tenn. Code Ann. § 48-58-301, is personally liable to the corporation.

Organizations that are exempt from federal income taxes are required to file a Form 990, Return of Organizations Exempt from Income Taxes, when their revenue is more than \$100,000. These forms were filed with the Court and exhibited in this trial. The form requires a list of names, addresses, titles and compensation. On forms 990 for the years ended 1994, 1995, 1996, 1997, 1998, John Madison was shown as the only director and that he was the Executive Director, that he worked 60 hours a week, and his compensation was \$52,000 a year.

Little People operated in several pieces of real property in Memphis, all owned by WillieAnn Madison. The street addresses for the facilities were 4933 Fairley and adjoining buildings, 2854 Mendenhall, Colony Park and 1647 Semmes. The personal residence of the Madisons was 1016 Twinkletown, Memphis, TN. WillieAnn Madison also owned a house in Mississippi, as well as a house at 1018 Twinkletown, Memphis, TN. The real property located at 1018 Twinkletown was transferred to William Davis, WillieAnn Madison's father and director of Little People, because Ms. Madison was concerned that Mr. Davis would not have a place to live following all of her child care related troubles.

During the years 1995, 1996, 1997, 1998 and 2001, WillieAnn Madison paid many of the personal expenses for herself, John Madison, their children and other relatives and family members from the bank accounts of Little People. In addition, some family members received salaries from Little People. The Plaintiff's expert witness, Mr. Larry Howlett, CPA, provided a summary of the expenditures at issue. The Court first looks at the nature of the expenditures concerning the family members as set forth in Trial Exhibit 53, starting with John Madison, and the Court must find and takes no pleasure in finding that the salary paid to John Madison was not authorized by the board of directors, but was simply decided by WillieAnn Madison. Section A of the summary shows, and there is no proof to the contrary, that Mr. Madison was paid \$307,664. The Court finds that Mr. Madison, Ms. Madison and William Davis will be responsible for refunding that amount, and that amount will be a part of the judgment that the Court hereby awards. That is also true for sums paid to Ms. Madison, Gloria Madison, Lawrence Madison, Anna Davis, Chris Daughtry, Chaun Daughtry, B. Madison, Brandy Daughtry and William Davis, which total \$604,998.33. The Plaintiff established that the board of directors did not approve the salaries and that Ms. Madison made those decisions.

As previously stated, the burden of proof to show the fairness of the conflict-of-interest transactions is placed upon Defendants John Madison and WillieAnn Madison because of their fiduciary duties as officers or directors. The Madisons were not able to show that the salaries paid were justified. The Court doesn't find that no work was done, but that the work that was done, in the main, unfortunately, was not for the benefit of the child care center, but was for the benefit of the family.

The Plaintiff showed that the mortgage or installment payments referenced in Section B of Trial Exhibit 53 were made to various banks to the personal benefit of WillieAnn Madison because she owned the real property on which the mortgage payments were made. Ms. Madison asserted at trial and in post trial papers that the payments were rent for space used by Little People and that the rental amounts were fair and reasonable. However, neither Ms. Madison nor Mr. Madison were able to show or did show that the board decided and made a decision about the rent that Ms. Madison would be receiving from the child care facility. Ms. Madison made that decision on her own, and Mr. Madison, the executive director, acquiesced after the fact.

There was no proof that other properties were considered for rental or lease by Little People, or that the particular property which was leased from WillieAnn Madison was a good site for the center, or that other sites were not more affordable or were not a better site for the childcare center. Ms. Madison, Mr. Madison, and William Davis carry the burden of proof on this issue; yet, they provided no proof that Ms. Madison or any other board member evaluated properties for purchase so that Little People could eventually own the property and accumulate equity.

Although it is clear that the purpose of the nonprofit organization is not to generate revenue, it is also very clear that Little People had to generate revenue in order to support itself, and accumulating equity and paying the lowest rent it could possibly pay for good property would be a reasonable goal and expected goal for a nonprofit. In fact in this case, the State showed that Ms. Madison continued to deal with her real property over the years so that Little People paid the amount that she wanted it to pay. The Court finds that the amount of rent that was charged, and therefore the amount of rent that was paid by Little People, was specifically for the purpose of enriching and supporting the Madison family.

The Court adopts the other identified payments set forth in Trial Exhibit 53 as findings by the Court unless otherwise excepted below. As for Section C, the Court finds that indirect payments to related entities totaled \$355,343.63 and are accurately summarized and should be awarded. The credit card amounts in Section D have already been awarded in summary judgment. As for Section E, the Court already awarded \$55,962 in summary judgment and hereby awards the additional amount of \$86,458.80. The Plaintiff did carry its burden to show that the insurance payments included in the exhibit were not made for the purpose of supporting the child care development center, but were made to insure the property and/or lives of the Madisons. As for Section F, the Court adopts that \$141,743.25 should be awarded. As for Section G, the Court awards the Plaintiff the amounts of \$41,575.67 paid to Nations Bank, the \$2,620.98 paid to PNC Bank, and the \$2,000 paid to Morgan; however, the Court finds that the \$20,000 noted as paid to Tri-State Bank has already been awarded in summary judgment. As for Section H, the Court accepts and awards the \$74,817.77 paid to various Memphis utilities. Under Section I, the Court awards the amount of \$67,408.28 and finds that Dr. James Proctor was the seller of the Mendenhall property and that Larry Weisman received the amount indicated as closing

costs. As for Section J, the Court awards \$50,264.57 and finds that said amount was paid for personal services to benefit the Madisons. Said amount was paid out of Little People's operating account and not charged by credit card. As for Sections K and L, the Court awards the \$17,993.52 and the \$8,850 amounts set forth in the respective sections. As for Section M, the Court finds that the medical expense figure has already been awarded in summary judgment. As for Section N, the Court awards \$8,200 and finds that said amount was paid to benefit the Madisons and their charities. As for Section O, the Court awards \$4,414.75....

The Court finds that the actions and conduct of Defendants WillieAnn Madison, John Madison, and William Davis were willful and wanton or were gross negligence. See, Tenn. Code Ann. § 48-58-601(c). The Court concludes that it is appropriate and hereby awards [a] judgment in the amount of \$1,782,666 against Defendants WillieAnn Madison, John Madison, and William Davis, joint[ly] and severally. Said amount represents the total summarized amount of \$2,213,205.13, less the stipulated amount of \$75,000 and the \$355,538.56 previously awarded by this Court in summary judgment. The amount now awarded in this Order shall be in addition to amounts previously ordered by this Court. It is further ordered that Defendants WillieAnn Madison and John Madison shall be liable for the amount adjudged against Defendant Phyllis D. Herring. Similarly, William Davis shall be deemed liable for all amounts previously awarded against Ms. Herring and the Madisons.

On October 27, 2006, this Court dismissed the Attorney General's claim for an additional \$2,228,491.30.⁸ Entry of this Order shall constitute final disposition of this matter by Tenn. R. Civ. P. 58.

Defendants appeal raising numerous issues. Defendants do not claim that they did not use the assets of Little People's for their personal gain. Rather, they challenge the amount or inclusion of certain items in the final judgment. The State also appeals, claiming the Trial Court erred when, in its order of October 27, 2006, it dismissed the State's claim for the value of the assets transferred to Preparatory Academy after Little People's was dissolved.

⁸ This additional \$2,228,491.30 claim represented amounts paid to Preparatory Academy and/or the Madison's after Little People's daycare license was transferred. See, Trial Exhibit 95. The Court took this claim under advisement at the October 11, 2006 hearing and later entered the aforementioned October 27, 2006 Order.

Discussion

Since all of the factual issues raised by Defendants pertain to the final judgment entered following trial, the standard of review set forth in Tenn. R. App. P. 13(d) applies. Thus, the factual findings of the Trial Court are accorded a presumption of correctness, and we will not overturn those factual findings unless the evidence preponderates against them. *See* Tenn. R. App. P. 13(d); *Bogan v. Bogan*, 60 S.W.3d 721, 727 (Tenn. 2001). With respect to legal issues, our review is conducted “under a pure *de novo* standard of review, according no deference to the conclusions of law made by the lower courts.” *Southern Constructors, Inc. v. Loudon County Bd. of Educ.*, 58 S.W.3d 706, 710 (Tenn. 2001).

Before we address the specific issues raised by Defendants, we will address the content of Defendants’ brief, which contains few citations to the voluminous record which fills three bankers boxes.⁹ With regard to the importance of citing to the record, Rule 27 of the Tennessee Rules of Appellate Procedure provides as follows:

Rule 27. Content of Briefs. - (a) Brief of the Appellant. - The brief of the appellant shall contain under appropriate headings and in the order here indicated:

* * *

(6) A statement of facts, setting forth the facts relevant to the issues presented for review *with appropriate references to the record*;

(7) An argument, which may be preceded by a summary of argument, setting forth the contentions of the appellant with respect to the issues presented, and the reasons therefor, including the reasons why the contentions require appellate relief, with citations to the authorities *and appropriate references to the record* (which may be quoted verbatim) relied on

Tenn. R. App. P. 27 (emphasis added).

The importance of citing to the record is further emphasized in Rule 6 of the Rules of the Court of Appeals, which provides, in relevant part, as follows:

Rule 6. Briefs. - (a) Written argument in regard to each issue on appeal shall contain:

⁹ Defendants’ were admonished by the Trial Court for their failure to cite to the record. This admonishment apparently went unheeded, or perhaps there was nothing else in the record favorable to Defendants’ issues.

(1) A statement by the appellant of the alleged erroneous action of the trial court which raises the issue and a statement by the appellee of any action of the trial court which is relied upon to correct the alleged error, *with citation to the record where the erroneous or corrective action is recorded.*

(2) A statement showing how such alleged error was seasonably called to the attention of the trial judge *with citation to that part of the record where appellant's challenge of the alleged error is recorded.*

(3) A statement reciting wherein appellant was prejudiced by such alleged error, *with citations to the record showing where the resultant prejudice is recorded.*

(4) A statement of each determinative fact relied upon *with citation to the record where evidence of each such fact may be found.*

(b) No complaint of or reliance upon action by the trial court will be considered on appeal *unless the argument contains a specific reference to the page or pages of the record where such action is recorded.* No assertion of fact will be considered on appeal *unless the argument contains a reference to the page or pages of the record where evidence of such fact is recorded.* (emphasis added)

In the recent case of *In re Estate of Price*, No. E2007-00523-COA-R3-CV, --- S.W.3d ---, 2008 WL 762489 (Tenn. Ct. App. March 24, 2008), *perm. app. denied Sept. 29, 2008*, we discussed the importance of complying with Tenn. R. App. P. 27.¹⁰ We stated:

In their appellate brief, Appellants allege that the Trial Court erred by refusing to impose a trust upon the assets of Ms. Price's Estate for the benefit and use of Mr. Fenner.

* * *

Plaintiffs neither cite any specific facts from the record in support of this bald assertion, nor do they attempt to explain why the Trial Court erred by failing to impose a trust upon the Estate.

¹⁰ *In re Estate of Price* will be published in the near future. At this time, only the Westlaw citation is available.

Rule 27 of the Tennessee Rules of Appellate Procedure specifies that an appellant's brief must contain, *inter alia*:

(7) An argument, which may be preceded by a summary of argument, setting forth the contentions of the appellant with respect to the issues presented, and the reasons therefor, including the reasons why the contentions require appellate relief, with citations to the authorities and appropriate references to the record (which may be quoted verbatim) relied on....

Tenn. R. App. P. 27(a)(7).

A party's failure to comply with the appellate brief requirements set forth in Tenn. R. App. P. 27 can have dire consequences, as we have warned repeatedly:

Courts have routinely held that the failure to make appropriate references to the record and to cite relevant authority in the argument section of the brief as required by Rule 27(a)(7) constitutes a waiver of the issue. *See State v. Schaller*, 975 S.W.2d 313, 318 (Tenn. Crim. App. 1997); *Rampy v. ICI Acrylics, Inc.* 898 S.W.2d 196, 210 (Tenn. Ct. App. 1994); *State v. Dickerson*, 885 S.W.2d 90, 93 (Tenn. Crim. App. 1993). Moreover, an issue is waived where it is simply raised without any argument regarding its merits. *See Blair v. Badenhope*, 940 S.W.2d 575, 576-577 (Tenn. Ct. App. 1996); *Bank of Crockett v. Cullipher*, 752 S.W.2d 84, 86 (Tenn. Ct. App. 1988).

* * *

As noted in *England v. Burns Stone Company, Inc.*, 874 S.W.2d 32, 35 (Tenn. Ct. App. 1993), parties cannot expect this court to do its work for them. This Court is under no duty to verify unsupported allegations in a party's brief, or for that matter consider issues raised but not argued in the brief. *Duchow v. Whalen*, 872 S.W.2d 692, 693 (Tenn. Ct. App. 1993) (citing *Airline Const. Inc., v. Barr*, 807 S.W.2d 247 (Tenn. Ct. App. 1990)).

Bean v. Bean, 40 S.W.3d 52, 55-56 (Tenn. Ct. App. 2000).

Plaintiffs failed to cite to any specific facts in the record supporting their argument that the Trial Court should have imposed a trust upon the assets of the Estate. Because Plaintiffs failed to comply with the requirements of Tenn. R. App. P. 27(a)(7), we hold that Plaintiffs have waived this issue on appeal.

In re Estate of Price, 2008 WL 762489, at *26.

Similarly, in *Bailey v. Champion Window*, 236 S.W.3d 168, 173 (Tenn. Ct. App. 2007), we stated:

The sections of the Baileys' brief dealing with their remaining issues contain nothing more than bare assertions that the Trial Court erred. These sections contain neither citations to the record showing where the alleged errors occurred, nor any argument or citations to case law or other authority indicating why the Trial Court may have been in error. The Baileys did not comply with the Rules of Appellate Procedure and the rules of this Court regarding these issues and, thus, have waived these issues on review. *See Bean*, 40 S.W.3d at 55.

Against this backdrop, we now discuss the specific issues raised by Defendants. In their first issue, Defendants claim that the Trial Court erred when it classified certain payments received by them and various family members as improper and illegal distributions that are subject to repayment. More specifically, Defendants claim that they and their family members were entitled to reasonable compensation for their services and the Trial Court failed to take that into account when rendering its judgment. In making this argument, Defendants cite us to their testimony showing the amount they (but not their family members) were paid over the years. What Defendants fail to do, however, is cite us to any proof showing that the amount they or their family members were paid over the years was reasonable or proper. Defendants do not offer this Court anything from which we could conclude that the amounts paid to them were reasonable or properly authorized by the nonprofit. The Trial Court specifically found that the Madison Defendants operated Little People's "as if it were their personal [for-profit] business." The Trial Court found that the salary paid to John Madison was not authorized by a board of directors, but simply was approved by Mrs. Madison. Importantly, the Trial Court also made the following factual determination:

As previously stated, the burden of proof to show the fairness of the conflict-of-interest transactions is placed upon Defendants John Madison and WillieAnn Madison because of their fiduciary duties as officers or directors. The Madisons were not able to show that the salaries paid were justified. The Court doesn't find that no work was done, but that the work that was done, in the main, unfortunately, was

not for the benefit of the child care center, but was for the benefit of the family.

On appeal, Defendants must show that the preponderance of the evidence weighs against this factual determination. In other words, they must show this Court that the preponderance of the evidence was such that the salaries were fair and the work was not done for the benefit of the Madison family. Simply stating on appeal that the amount paid to the Madisons was fair, with virtually no cites to the record or discussion of any actual evidence in support of this assertion, is altogether insufficient.

As a similar but separate issue, Defendant John Madison claims that he should have been paid a reasonable compensation for his accounting services and that this reasonable amount should be deducted from the judgment. From the record, it appears that John Madison did very little, if any, accounting work *that actually benefitted the nonprofit*. For example, he knew that the assets from Little People's were being used for years for the payment of personal expenses for practically his entire family, *including himself*. He did nothing about this situation. He certainly did not stop this improper and illegal behavior. He consistently failed to follow reasonable accounting principles. Importantly, once again there are no citations to the record for most of the facts which John Madison claims support his argument that he should be compensated for accounting work that he claims benefitted the nonprofit. He has failed to demonstrate that the facts preponderate against the Trial Court's finding that any actual work that may have been performed by John Madison did not benefit the nonprofit. Thus, the Trial Court's judgment with respect to this issue is affirmed.

The next issue is Defendants' claim that the rent paid by Little People's should not be included in the judgment because the payment of rent was a legitimate expense of the nonprofit. Again, Defendants fail to cite us to anything in the voluminous record that would support a conclusion that the facts preponderate against the Trial Court's findings relevant to this issue. Defendants acknowledge that the payment of rent comprised a staggering total of \$1,440,000¹¹ for the various properties over a five year period. As set forth above, with respect to the payments made by Mrs. Madison for "rent," the Trial Court found:

The Plaintiff showed that the mortgage or installment payments referenced in Section B of Trial Exhibit 53 were made to various banks to the personal benefit of WillieAnn Madison because she owned the real property on which the mortgage payments were made. Ms. Madison asserted at trial and in post trial papers that the payments were rent for space used by Little People and that the rental amounts were fair and reasonable. However, neither Ms. Madison nor Mr. Madison were able to show or did show that the board decided and made a decision about the rent that Ms. Madison would be receiving from the child care facility. Ms. Madison made that

¹¹ Defendants do not refer to this amount as "staggering"; but this Court does.

decision on her own, and Mr. Madison, the executive director, acquiesced after the fact.

There was no proof that other properties were considered for rental or lease by Little People, or that the particular property which was leased from WillieAnn Madison was a good site for the center, or that other sites were not more affordable or were not a better site for the childcare center. Ms. Madison, Mr. Madison, and William Davis carry the burden of proof on this issue; yet, they provided no proof that Ms. Madison or any other board member evaluated properties for purchase so that Little People could eventually own the property and accumulate equity.

Although it is clear that the purpose of the nonprofit organization is not to generate revenue, it is also very clear that Little People had to generate revenue in order to support itself, and accumulating equity and paying the lowest rent it could possibly pay for good property would be a reasonable goal and expected goal for a nonprofit. In fact in this case, the State showed that Ms. Madison continued to deal with her real property over the years so that Little People paid the amount that she wanted it to pay. The Court finds that the amount of rent that was charged, and therefore the amount of rent that was paid by Little People, was specifically for the purpose of enriching and supporting the Madison family.

Defendants again offer this Court nothing to show that the preponderance of the evidence weighs against these findings. Defendants cite us to no evidence showing or even suggesting that the amount of rent paid was either proper or authorized. In their brief, Defendants state:

WillieAnn Madison testified that, in some cases, she charged Little People's a rental fee which was less than the fair market rental value estimated on the appraisal for the property. Thus, Appellants assert that the rental contracts or leases were fair and reasonable. Rental payments were owed and paid in the amount of \$1,440,000 and this amount should be subtracted from the judgment amount awarded.

Defendants' conclusory allegations do not cite us to anywhere in the record where we can find such testimony. Even if such citations were made, the preceding argument does not explain how much of the total judgment was comprised of rental payments made on property where Ms. Madison claims she charged less than the fair market rental value. The preceding does nothing to address the Trial Court's finding that there was no proof that the properties that were "rented" were proper sites for the childcare centers, as compared to other less expensive and available properties.

Defendants do not cite us to where the alleged appraisals are located in the record, if at all. Defendants essentially state only that a nonprofit can pay rent, and that \$1,440,000 was the amount of rent paid. This is altogether insufficient and does not even begin to show that the preponderance of the evidence weighs against the Trial Court's findings. Accordingly, we affirm the judgment of the Trial Court on this issue.

Defendants next claim that the Trial Court erred when it failed to deduct from the judgment utility payments made at the facilities Little People's was "renting." In the "Facts" section of Defendants' brief, the following is stated with regard to the utility payments:

In order for Little People's to operate, payments had to be made for necessary utilities. These payments were made to Memphis Light, Gas and Water. No evidence was presented to show that these payments were excessive, unfair or unreasonable.

The foregoing, obviously, contains not one citation to the record. In the "Argument" section of Defendants' brief, they state: "Many of these [utility] payments were made for utilities provided to the properties utilized in running Little People's." Again, no citations to the record.

The Trial Court awarded damages for \$74,817.77 representing improper utility payments. The evidence shows that the nonprofit paid the utility payments for the Madisons' personal residence, as well as apartments where relatives were living, etc. Little People's also paid utilities for non-company related utility expenses in the State of Mississippi. Defendants cite us to nothing showing how much of the \$74,817.77 they claim should be considered proper and why.

The State, however, has provided this Court, by citation to the record, with a detailed list of some of these improper utility payments including, but not limited to, payment by the nonprofit of \$1,789.46 to North Central Mississippi Electric, and payments of over \$7,000.00 to Memphis Light Gas & Water for the Madisons' personal residence. Because Defendants have failed to provide citations to the record and further have failed to establish that the facts preponderate against the Trial Court's findings, the Trial Court's judgment on this issue is affirmed.

Defendants argue that \$6,489.09 in rent inadvertently was overpaid on property WillieAnn Madison purchased from James Proctor, and they should receive a credit for the amount of the overpayment. According to Defendants:

James Proctor testified that he is able and willing to repay the overage, but was advised by the Attorney General's Office not to repay this sum. This amount was not deducted from the rent expenditures paid out and was attributed to Appellants as part of the Chancery Court's judgment.

Once again, Defendants cite us to nowhere in the three bankers boxes comprising the record where this information can be found. Defendants do not cite to Proctor's alleged testimony. This issue is, therefore, waived.

The next issue is a claim by Mr. Madison that the Trial Court erred when it found him jointly and severally liable for the actions of his wife.¹² Mr. Madison's argument is as follows:

John Madison [is] not responsible for the action of Little People, because [he] did not ratify or provide assent to the actions. Although a breach of fiduciary duty has been alleged, John Madison . . . [was] not shown to permit mismanagement. A director is only liable to the corporation if he votes for or assents to a distribution made in violation of the nonprofit corporation statutes. Tenn. Code Ann. § 48-58-301; *Summers v. Cherokee Children & Family Servs.*, 112 S.W.3d 486 (Tenn. Ct. App. 2002).

John Madison did not personally receive significant tangible or other benefits. . . . The [e]vidence also shows that WillieAnn Madison unilaterally signed and approved the leases. Thus, WillieAnn Madison should be held solely liable, at a minimum, for any rental values . . . owed by Little People's.

Even if John Madison is liable for a breach of fiduciary duty as contemplated under Tennessee Law, Tennessee Law does not provide a measurement for the extent of their liability. Although, some states may have held that a fiduciary cannot protect himself by arguing they were merely a figurehead, Tennessee Courts have no case law on this defense. Thus, John Madison asserts that the extent of any liability placed upon [him] should not exceed the amount [he] personally benefited (sic).¹³

¹² This final issue also contains a claim that the Trial Court erred when it found defendant William Davis jointly and severally liable. However, as mentioned previously at footnote 1, Mr. Davis' notice of appeal was defective and was dismissed, and so we will not consider the portion of this issue directed to William Davis. When quoting from Defendants' brief, we omitted the portion of the argument pertaining solely to William Davis.

¹³ The State disagrees with the claim by Defendants that there is a lack of Tennessee law as to whether a director can successfully claim that he was merely a figurehead and avoid liability. In *Neese v. Brown*, 405 S.W.2d 577 (Tenn. 1964), the Tennessee Supreme Court indicated that, by becoming a director, that director agrees to being more than a mere figurehead. According to *Neese*:

Directors, by assuming office, agree to give as much of their time and attention to the duties assumed as the proper care of the interests intrusted to them may require. If they are inattentive to their duties, if they neglect to attend meetings of the board,

(continued...)

The above quoted argument by Defendants contains absolutely no citations to the record. Interestingly, the only fact mentioned in the “Facts” section of Defendants’ brief bearing on this issue is the following statement: “Little People’s Board members were aware of Mrs. Madison’s lease transactions with the corporation.” Since Mr. Madison was a board member, this statement seems to be directly contrary to his present argument that he did not assent to the rental transactions between Little People and WillieAnn Madison. This is even more apparent when you consider that, in the “Facts” section of Defendants’ brief, they state:

From 1995 to 2000, a period of approximately six (6) years, Appellant John Madison, Mrs. Madison’s husband and a certified public accountant, contracted with Little People’s to provide bookkeeping and other financial, payroll, recordkeeping and management services

Thus, Mr. Madison freely admits that he was a certified public accountant providing accounting services for the nonprofit, and that he knew of the lease agreements. In short, John Madison’s own brief supports the Trial Court’s finding that he knew about and assented to the improper conduct of his wife. More importantly, however, John Madison cites us to absolutely no evidence that would support his bald assertion that: (1) he did not “ratify or provide assent to the actions” of WillieAnn Madison and (2) he was not shown to have “permit[ted] mismanagement.” Mr. Madison does not even bother to cite to his own testimony which might pertain to this issue.

The Trial Court found that John Madison assented to the mismanagement by WillieAnn Madison, and that he personally benefitted from this assent. The Trial Court also held that Tenn. Code Ann. § 48-58-304 provides that a director who assents to a distribution made in violation of the Nonprofit Corporation Act, and who does not comply with the standards of conduct established in the Act is personally liable to the corporation. In pertinent part, Tenn. Code Ann. § 48-58-304(a) provides that:

¹³(...continued)

if they turn over the management of the business of the company to the exclusive control of other agents, thus abdicating their control, then they are guilty of gross neglect with respect to their ministerial duties, and, if loss results to the corporation by breaches of trust or acts of negligence committed by those left in control, which by due care and attention on their part could have been avoided, they will be responsible to the corporation. The diligence required from them has been defined as that exercised by prudent men about their own affairs, being that degree of diligence characterized as ordinary. If a less degree of diligence is exercised, the negligence is gross, and for losses consequent he is liable. ‘What constitutes a proper performance of the duties of a director,’ says Mr. Morawetz, ‘is a question of fact, which must be determined in each case in view of all the circumstances, - the character of the company, the condition of its business, the usual method of managing such companies, and all other relevant facts must be taken into consideration.’ Mor. Priv. Corp. § 552.

Neese, 405 S.W.2d at 580-81 (quoting *Wallace v. Lincoln Savings Bank*, 15 S.W. 448, 453-54 (Tenn. 1891)).

Unless the director complies with the applicable standards of conduct described in § 48-58-301, a director who votes for or assents to a distribution made in violation of chapters 51-68 of this title or the charter is personally liable to the corporation for the amount of the distribution that exceeds what could have been distributed without violating chapters 51-68 of this title or the charter.

In short, the Trial Court found that as the nonprofit's Executive Director and accountant, John Madison assented to all of the illegal conduct of his wife. Mr. Madison has not shown this Court anything in the record that is contrary to the Trial Court's finding. Even if there was some proof of lack of assent, Mr. Madison still would have to establish that those facts preponderate against the facts detailed by the Trial Court when it found that Mr. Madison did assent to his wife's conduct. In addition, Mr. Madison would have to show "the amount of the distribution that exceeds what could have been distributed without violating chapters 51-68 of this title or the charter." Tenn. Code Ann. § 48-58-304(a). Mr. Madison has ignored this statutory requirement altogether in his brief on appeal. Because Mr. Madison had failed to establish that the preponderance of the evidence weighs against the Trial Court's findings on this issue, the judgment of the Trial Court is affirmed as to this issue.

Defendants' failure to cite to the record in their brief on appeal did not escape notice by the State. The following is taken from the State's brief:

The Madisons failed to make proper "references to the record" although clearly required by the Rules of Appellate Procedure. . . . Numerous contested facts are presented in Appellants' statement of facts and elsewhere in their brief without any citation to the record. . . . Legal arguments are set forth without "citations to authorities" relied upon. . . . On several occasions, the Appellants cited to the opening statements of trial counsel. . . . Such statements are not a substitute for the pleadings or for evidence. See *Harris v. Baptist Memorial Hospital*, 574 S.W.2d at 732. . . . The Madisons failed to make any showing that the asserted errors were raised below. . . .

Notwithstanding the State having emphasized the fatal flaws of Defendants' brief, Defendants did not request permission to file a new or supplemental brief which complied with the Rules of Appellate Procedure or the Rules of the Court of Appeals. After considering the various issues raised by Defendants, all of those issues are found to be without merit, and the judgment of the Trial Court with respect to all of the issues raised by Defendants is affirmed.

As mentioned previously, the State raises one issue on appeal.¹⁴ Specifically, the State claims that the assets and other profits usurped and transferred by the Madisons to their newly created limited liability company, the LLC, should have been included in the Trial Court's judgment. In its October 2006 order, the Trial Court concluded that to the extent Little People's license may have been used post-dissolution by the Madisons to receive state or federal funds, there was no injury to the State because those child care services were provided. While this technically may be true, the State's claim is much broader than simply trying to recoup state money that may have been improperly used by Preparatory Academy or the Madisons. More specifically, the State also is trying to recover the value of the nonprofit at the time it was dissolved. In the final judgment quoted at length above, the Trial Court made this specific finding: "The Court also finds that Little People's nonprofit assets were transferred to the Preparatory Academy." These "assets" are what the State is trying to recover.

The case of *Summers v. Estate of Ford*, 146 S.W.3d 541 (Tenn. Ct. App. 2004) is similar to the present case in many respects. The *Summers* case was filed by the Tennessee Attorney General seeking to recover assets of a nonprofit public benefit corporation known as Children's Palace Learning Academy ("CPLA"), which operated child daycare centers in Memphis. *Id.* at 543. The nonprofit in *Summers* was established by Dr. James Ford to provide daycare for underprivileged children. As in the present case, it was alleged (and proven) that nonprofit assets were used for the private benefit of the nonprofit's founder. One of the State's claims sought recovery of nonprofit assets that eventually were transferred to one or more limited liability companies. The trial court in *Summers* determined that the nonprofit was entitled to the return of the value of the nonprofit that was transferred. *Id.* at 578-79. On appeal, this Court agreed. We stated:

The trial court ruled that "[t]he four daycare center businesses known as 'Children's Palace Learning Academy,' are the property of Children's Palace Learning Academy, a Tennessee nonprofit corporation; including the tangible assets, streams of income from the State, the goodwill, and the things listed as business assets." On appeal, the Estate contends that this holding was in error. We disagree. We affirm the Final Order of the probate court to the extent that it finds that the tangible and intangible assets of CPLA are CPLA property. In addition, we find that any income or property, belonging to CPLA, that was transferred, pursuant to the March 19, 2002, or any subsequent, Order, to any of the LLC[s] should also be awarded to CPLA. Although the LLCs may continue to function as separate entities, based upon our discussion above, they have no right to any CPLA property, money, license, etc. We remand for such further proceedings as may be necessary to determine the extent of transfers of CPLA property to the LLCs.

¹⁴ In addition to not filing a new or supplemental lead brief, Defendants also chose not to file a reply brief or to make any response whatsoever to the issue raised by the State.

Id. at 578-79.

In its well-considered and thorough final judgment, the Trial Court painstakingly attempted to determine the amount of nonprofit assets that had been pillaged by the Madisons and to award a judgment to the State on behalf of the nonprofit for that amount. With the award of that judgment, the Trial Court returned the parties to the pre-dissolution status quo. At that particular point in time, the nonprofit was still a viable corporation that unquestionably had some value, as evidenced by the millions of dollars the Madisons had improperly taken from the nonprofit over the years.

This final issue advanced by the State is simply its attempt to recoup what remained of the nonprofit when the assets of Little People's were transferred to the LLC. This claim was set forth clearly in the complaint as follows:

Upon information and belief, nonprofit assets of defendant Little People have inured to the private benefit of John Madison and WillieAnn Madison, both directly and indirectly through defendant Preparatory Academy.

Defendant Preparatory Academy is currently operating a child care agency at 4933 Fairley and 2845 Mendenhall. Nonprofit assets of defendant Little People have been improperly transferred to the custody or control of defendant Preparatory Academy without the approval of the Attorney General. Said assets are currently being utilized for its private benefit. Such transfer was outside the regular course of defendant Little People's activities.

As we did in *Summers*, we hold here that the State is entitled to a judgment against Defendants for both tangible and intangible assets of Little People's that were transferred, sold, or otherwise disposed of upon the dissolution of Little People's. This is nothing more than returning the property of Little People's to it. To the extent the October 27, 2006, order of the Trial Court is inconsistent with the foregoing, we reverse and "[w]e remand for such further proceedings as may be necessary to determine the extent of transfers of [Little People's] property to the [LLC]." *See Summers*, 146 S.W.3d at 578-79.

Conclusion

The judgment of the Trial Court is affirmed in part and reversed in part. This cause is remanded to the Trial Court for further proceedings consistent with this opinion and for collection of the costs below. Costs on appeal are taxed to the Appellants, WillieAnn Madison and John Madison, and their surety, for which execution may issue, if necessary.

D. MICHAEL SWINEY, JUDGE